BRIEF IN SUPPORT OF PETITION.

Argument.

POINT I.

The functions of a statutory committee are not similar to those of a committee appointed under §44(b) in ordinary bankruptcy. The allowable expenses of a statutory committee should not be limited to those incurred by it in passing judgment on the plan and in making that judgment known to the debtor and creditors.

The lower court, in its opinion, has held that the committee referred to in §338 of the Bankruptcy Act corresponds to the committee authorized under §44(b). In that connection the court, in its opinion, cited with approval Judge Chestnut's opinion in the *Matter of Credit Service, Inc.,* 31 F. Supp. 979. This holding of the lower court has created so much uncertainty as to the true function of the Statutory Committee and its proper place in the Arrangement proceeding as to justify a careful examination of that problem.

Contrasting the committee appointed in bankruptcy liquidation, provided for in Chapters I to VII, and the committee in Arrangements, Chapter XI, we find that §44(b), which defines the functions of the bankruptcy committee (we use this phrase to distinguish it from the Statutory Committee in Arrangement proceedings), provides that that committee may

(1) consult and advise with the trustee in connection with the administration of the estate;

(2) make recommendations to the trustee in the performance of his duties; and

(3) submit to the court any question affecting the administration of the estate.

The functions of the bankruptcy committee are thus clearly defined. In the great majority of proceedings filed under the Arrangement statute, the Arrangement proceeding is initiated as an original proceeding. That is to say, that although provision is made (§321) for filing an Arrangement petition in a pending bankruptcy proceeding, in actual practice §321 has been invoked in comparatively few cases. Therefore, in only a few cases is there a trustee serving at the time when an Arrangement proceeding is initiated.

§338 provides that if a trustee has not been previously appointed, creditors may nominate one at the first meeting of creditors, "who shall thereafter be appointed by the court in case it shall become necessary to administer the estate in bankruptcy". In other words, the trustee's office does not come into being unless and until it becomes necessary to administer the case in bankruptcy.

Since there is no trustee with whom the Arrangement Committee can consult or advise or to whom the Committee can make recommendations, the only function of the bankruptcy committee, therefore, that can possibly be said to have any application in an Arrangement proceeding if "the functions and obligations of the committee" "correspond to the committee authorized by §44(b)" is the third item of the latter section, which provides that the committee may submit to the court any question affecting the administration of the estate.

It is clear, however, that Congress could not have intended so narrow and tenuous a position for the Arrangement committee, for, otherwise, there would have been no necessity for providing in §337(2) for "the actual and necessary expenses incurred in connection with the proceedings *and the arrangement* by the committee of creditors and the attorneys or agents of such committee".

It would seem that if the exclusive function of the Statutory Committee in an Arrangement proceeding is merely to submit to the court any questions affecting the administration of the estate, there was no reason for providing for the actual and necessary expenses incurred in connection with the proceeding and the arrangement (1) by the committee of creditors, (2) by the attorneys, or (3) by the agents of such committee.

Perhaps we are laboring this point unnecessarily but it does seem from an examination of the Arrangement statute that it could not possibly have been the intent of the framers of this legislation that the functions of the Arrangement committee corresponded to the functions of the bankruptcy committee. Once this premise is accepted, it is appropriate to examine §§337 and 338 to determine the intent of Congress in the provisions for the Arrangement committee.

As we have already pointed out, in the normal Arrangement proceeding there is no trustee and except in unusual cases, where a receiver or custodian is appointed (§332), there is no officer of the court charged with the responsibility of supervising the proceeding. Certainly that is not within the province of the referee, who, under the statute, is the court (§1(9)). It would seem that the Arrangement committee, provided for in Chapter XI, is the only de-

vice by which there can be imparted to an Arrangement proceeding an adversary character.

This court has commented on this precise deficiency in Chapter XI in *Securities & Exchange Commission* v. *United States Realty & Improvement Company,* 310 U. S. 434, at page 450. In that case Mr. Justice Stone, in the course of his opinion, contrasting the protective provisions of Chapter X with those of Chapter XI, said:

> "No comparable safeguards are found in chapter XI. Every phase of the procedure bearing on the administration of the estate and the development of the arrangement is under the control of the debtor. The process of formulating an arrangement and the solicitation of consent of creditors, sacrifices to speed and economy every safeguard, in the interest of thoroughness and disinterestedness, provided in chapter X. The debtor is generally permitted to stay in possession and operate the business under the supervision of the Court, §342, 11 USCA §742, and a trustee is provided for only in the case where a trustee in bankruptcy has previously been appointed and is in possession, or if 'necessary' a receiver may be appointed. §332, 11 USCA §732. The debtor proposes the arrangement, §§306(1), 323, 357, 11 USCA §§706(1), 723, 757, and the only opportunity afforded the creditors in respect to the proposed plan is to accept or reject it as submitted by the debtor."

Further on in his opinion, at page 451, Mr. Justice Stone said:

> "There are no provisions for an independent study of the debtor's affairs by court or trustee,

> or for advice by them to creditors with respect to their rights or interests in advance of their consent to the arrangement. Committees of the creditors are permitted, §§334, 338, 11 USCA §§734, 738, but there is no restriction on or supervision over their selection and conduct as in chapter X. The arrangement may be consummated at the conclusion of a single creditors' meeting. The Court in passing upon the arrangement, is without the benefit of investigation and study by the trustee or Commission, which Congress has required in reorganization proceedings under chapter X, and is then faced with the fact that a majority of the creditors have already accepted the plan."

It would seem clear that the function of the Statutory Committee in an Arrangement proceeding was intended by Congress to be much broader and much more substantial than that of the bankruptcy committee (§44(b)), which is only auxiliary to the trustee.

We respectfully submit that this court is faced with the problem of interpreting Chapter XI of the Act so as to constitute it a medium for orderly and effective administration. It would seem clear that if the function of the Statutory Committee is merely to submit to the court any questions affecting the administration of the estate, then it is only in connection with this function that the attorneys and agents may be employed and compensated and it is only in connection with this function that the actual and necessary expenses incurred could be recovered. The greater part of the services of the committee intended under the Arrangement statute, even when performed by attorneys and agents, must go unrewarded under this narrow interpretation. This, in

turn, means either that the door is open in Arrangement proceedings to extensive fraud and chicanery on the part of the debtor or to the unrestricted appointment of receivers so that some measure of supervision and control over the debtor's affairs can be had while the proceeding is pending.

There would seem to be no logical argument against the Arrangement committee taking an active part in the conduct of the administration of the estate. There is no good reason why the committee should not have an active voice in the supervision and continuation of the debtor's business during the time that the Arrangement proceeding is pending. The Committee should have the right to conduct examinations to determine whether the debtor has committed any act which would bar his discharge since under §366(4) the commission of such act would prevent confirmation of an Arrangement (see also §366(5)). However, to say that services of this kind must go unrewarded is to say, in effect, that they will not be performed.

This court, without doing violence to any of the provisions of the statute and within the language thereof, can and should define the functions of the Arrangement committee sufficiently broadly so as to permit the committee to perform the functions set forth in the petition herein (p. 11).

The lower court has held (p. 221) that the allowable expenses of the Statutory Committee "must be limited to those incurred by it in passing judgment upon the plan and in making that judgment known to the debtor and the creditors for appropriate action by him or them".

We have already noted the conspicuous omission in the provisions of Chapter XI for imparting an

adversary character to Arrangement proceedings unless §§337 and 338 are liberally construed. The functions of the committee, as defined by the lower court, exclude it from participation in a variety of matters which arise during the course of the proceeding. In a majority of cases the debtor is continued in possession. Unless the committee is given some voice in the actual running of the business, creditors in many cases will have no recourse other than the application for the appointment of a receiver, with the attendant expense that such a step would entail. It is unreasonable to expect individual creditors to assume the burden of supervising the proceeding, including the retention of attorneys and accountants.

The committee is admirably suited to perform this function and we respectfully submit that without doing violence to any of the provisions of the statute and within the language thereof, this court should interpret the functions of the committee as we have indicated hereinabove.

This court has pointed out in *United States* v. *Hutcheson,* decided Feb. 3, 1941, 85 L. Ed. 424 at 426, "the importance of giving 'hospitable scope' to Congressional purpose even when meticulous words are lacking".

The lower court has expressly excluded the services rendered by agents of the Statutory Committee in the active solicitation of assents to the proffered plan on the ground that these are tasks within the compass of the Committee's own duty or are rendered on behalf of the debtor. This, we submit, is not a correct statement of fact. The consummation of the plan is, of course, of interest to the debtor

since the fact that the debtor offers the plan is an indication of the fact that it regards the consummation thereof to be in its own interest. Once a satisfactory plan has been negotiated, however, the consummation thereof is just as much in the interests of creditors as in that of the debtor.

POINT II.

The services rendered prior to the Statutory Committee's appointment by persons who the Committee makes its agents and whose services are of value in the administration of the estate are properly compensable.

The lower court has held that "expenses incurred prior to the Committee's appointment are not allowable since they are designed to facilitate advance acceptance of the plan rather than to aid impartial judgment upon it".

In point of fact, services rendered before the Committee's appointment, in the majority of cases, are by no means designed to facilitate advance acceptance of the plan. In practice, in the great majority of cases, the negotiations that precede the election of the Arrangement committee are devoted to an examination into the debtor's affairs with a view to a determination of whether the Plan, which has been filed simultaneously with the petition initiating the proceeding (§323), is fair. Such examination is not usually confined solely to an investigation as to whether a liquidation of the existing assets would result in a more favorable distribution to creditors than the provisions of the proffered plan. They extend to a consideration of the prior history and

conduct of the debtor. Express provision for this phase of the administration in a Reorganization Proceeding is contained in Chapter X (§167). Notwithstanding the absence of a comparable section in Chapter XI, it would seem that the committee of creditors should be permitted to perform this precise function, which either the trustee or examiner would perform in a Chapter X proceeding. The examination into the prior history and conduct of the debtor is as important in an Arrangement proceeding (see §366(4)) as it is in a Chapter X proceeding or in an ordinary liquidation proceeding. The payment of preferences and fraudulent transfers prior to bankruptcy may have a material bearing on whether a plan is fair. So has the question of whether the debtor is entitled to a discharge. Study and investigation must be made of such situations and the plan weighed in the light of possible realization on causes of action. Who is to perform these services in an Arrangement proceeding unless the Statutory Committee is the agency through which they shall be performed? The lower court's characterization of these prior services as "designed to facilitate advance acceptance of the plan rather than to aid impartial judgment upon it", is, we submit, unrealistic and overlooks the essential functions which the preliminary investigation serves.

In concluding this point, we take the liberty of emphasizing the limitations that have been imposed on the Statutory Committee's functions if it cannot be paid for services rendered by its agents prior to the appointment of the Committee. It requires no extended discussion to make the point that the sooner investigation and examination are undertaken in the ordinary case the greater the chance of detecting fraud. If the Committee cannot receive re-

imbursement for its expenses for services rendered prior to its official appointment, its natural inclination would be to allow matters to rest until the first meeting. That may mean an interval of anywhere from ten days to three weeks (§334), depending on how soon the referee calls a first meeting of creditors. There can be no logical reason for refusing reimbursement to the Statutory Committee's agents for services rendered prior to its appointment where such agent's work if adopted not only contributed materially to the Committee's efforts but where the work would have had to be performed after the election of the Committee, if it had not already been completed. For example, why should the Committee be refused reimbursement for the expense of an accountant, who worked from the time of the filing of the petition down until the time when the Committee was elected? To be sure, if the accountant did the same work after the election of the Statutory Committee it would seem that his services would properly fall under §337(2). Nevertheless, the effect of the lower court's decision is to delay the commencement of the accountant's services until the appointment of the Statutory Committee, during which time important records might disappear or be altered with consequent substantial prejudice to the statute.

An official committee, which engages the services of agents before its election as an official committee, runs a two-fold risk: (1) that eventually it may not be elected the Statutory Committee; and (2) that the services of its particular agents may not be construed by the referee as having contributed to the eventual result. Although these are risks which the agents of the unofficial Committee must assume, there is no good reason for placing further deterrents upon the rendition by them of essential services.

The decision of this type of application should turn on the facts in each particular case. The referee observes at first hand every important step in an Arrangement proceeding. He is eminently qualified to decide whether the services performed before or after the appointment of a Statutory Committee are deserving of compensation. He should be given this discretion free of the arbitrary rule of chronology which prevents compensation for services rendered before the appointment of the Committee, regardless of their place in the entire administration.

The lower court, in arriving at its decision, has enunciated certain rules which affect the administration of Arrangement proceedings in substantial measure. We submit that these rules as enunciated do not state the intendment of Congress in the enactment of the Arrangement statute and we urge most earnestly upon this Court that a careful reexamination of the Statutory Committee's functions in Arrangement proceedings is both necessary and desirable to prevent injustice and to insure a structure within the confines of which the Arrangement statute can serve the purpose for which it was enacted.

CONCLUSION.

In order to resolve the grave doubt as to the correctness of the decision below and to furnish a guide in the administration of Arrangement proceedings, it is respectfully submitted that the writ of certiorari should be granted.

Respectfully submitted,

SYDNEY KRAUSE,
Counsel for Petitioners.